



# Economic Indicators

Prepared by the Department of Finance • December 2004

*The purpose of this report is to keep policy makers apprised of changes in the national and local economies that the Montgomery County Department of Finance believes may impact current and/or future revenues and expenditures.*



*This report is also available through the Internet on the Montgomery County Web Page:  
<http://www.montgomerycountymd.gov>*

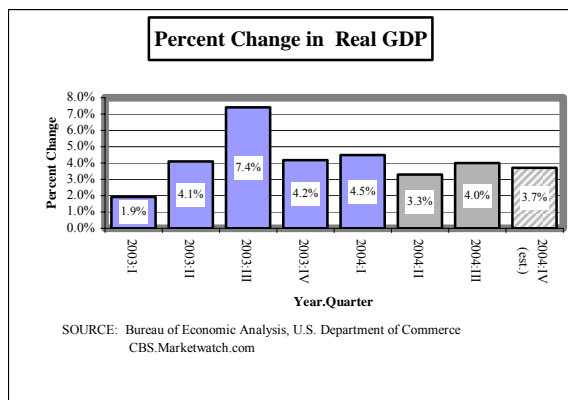
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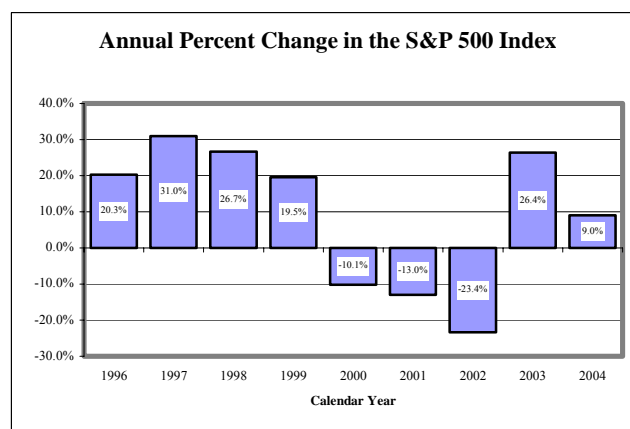
## ECONOMIC OVERVIEW

The national economy continued to strengthen in 2004 with a 4.0 percent increase in real GDP during the third quarter and 3.9 percent for the year. Consumption of durable goods was up 17.2 percent during the quarter (↑6.1% for the year), residential construction increased 1.6 percent (↑7.5% for the year), and business investment in new equipment rose 17.5 percent (↑13.2% for the year) during the quarter. To date, business investment led the expansion in 2004 compared to residential investment during 2003. According to a survey of 55 economists by the *Wall Street Journal*, the U.S. economy will see a modest but healthy growth of 3.7 during the fourth quarter of 2004 and 3.6 percent in 2005, both slightly less than the 3.9 percent during the first three quarters of 2004. According to fourth quarter “advance” estimates released by the Bureau of Economic Analysis (BEA), GDP grew 3.1 percent during the fourth quarter. However, BEA stated that the “advance” estimate is based on incomplete data and will be subject to further revisions in February and March.



While the stock market ended the year on a positive note, all of the gains occurred during the last two months of the year. Compared to the results in the prior year, the stock market was not a stellar performer.

While the economy grew 3.9 percent for the first three quarters of 2004, two of the four major stock indices were below their December 2003 levels, one had virtually no change, and the fourth had a modest gain. The Dow Jones Industrial Average was down 3.6% and the NASDAQ was 5.3 percent below its December level. The broader S&P 500 index, which was up 0.2 percent, changed very little from December 2003, and the Russell 2000 index was up a modest 2.9 percent, only 90 basis points above a six-month Treasury bill.



However, during the fourth quarter of 2004, the stock market made a significant recovery such that all four indices turned positive by yearend. The Dow Jones was up 7.0 percent ending the year at 3.2 percent, the NASDAQ and Russell 2000 indices increased a remarkable 14.7 percent and 13.7 percent, respectively, during the quarter ending at 8.6 percent and 17.0 percent, respectively, for the year. The S&P 500 also rebounded during the fourth quarter ending at a 9.0 percent gain for the year.

Short-term interest rates rose in response to the Federal Reserve’s policy of raising the target on federal funds 125 basis points during the second half of 2004 to 2.25 percent by the end of 2004. While the Fed raised the rate on federal funds during this

period, the interest rate on the bellwether 10-year Treasury bond actually declined from 4.6 percent at the end of June to less than 4.2 percent by the end of the year.

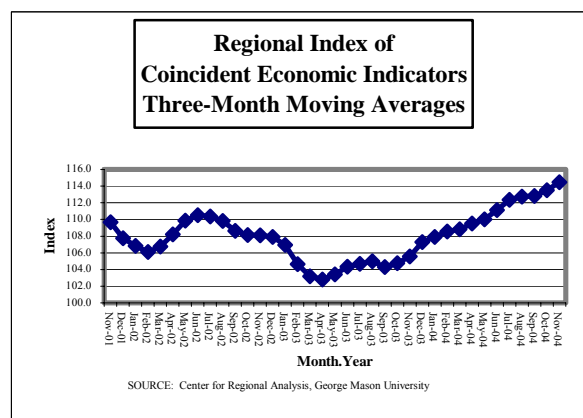
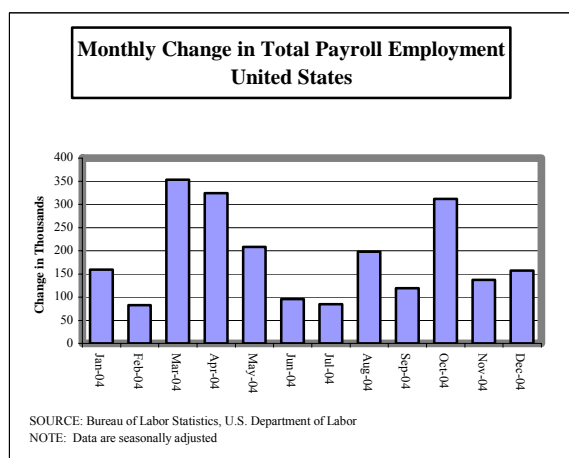
Because 30-year mortgage rates are closely associated with the 10-year Treasury bond, mortgage rates were below the 6 percent threshold through the latter part of 2004. Because of such historically low rates, the real estate market continued to be the success story of 2004. In the final month of 2004, housing starts ended the year at an annual rate of 2.0 million units. While that rate was 3.0 percent below December 2003, housing starts were up 5.1 percent for the year. At an average annual rate of 2 million units, that rate was the largest since 1978. Housing sales increased an estimated 9.4 percent in 2004 based on preliminary data, which followed a 9.6 percent increase in 2003.

With the expansion of the economy, a rebound in the stock market during the fourth quarter, and a strong housing market, the number of jobs added to payroll employment was over 2.2 million in 2004, with the service-providing sectors adding 1.9 million of those jobs. This was the strongest showing of new jobs since 1999.

Because of the strong economy and payroll employment gains, consumer confidence was generally optimistic in 2004. The University of Michigan Survey of consumer sentiment also revealed an optimistic outlook in 2004. However, consumer expectations about the future were less than optimistic.

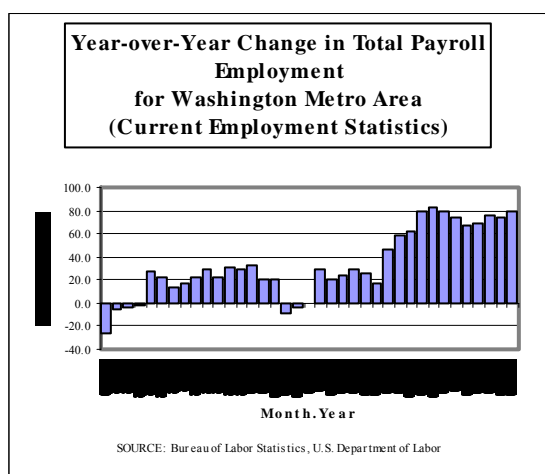
It is against the national economic backdrop that the economic performance of the Washington metropolitan statistical area and Montgomery County is analyzed. According to the Center for Regional Analysis (CRA), the region's economy exhibited strong performance in 2004 attributed largely to federal spending.

The Washington Coincident Index, a measure of the current state of the region's economy, decreased 1.1 percent in November. Despite that decrease and based on a three-month moving average, the index has increased 8.4 percent over the past twelve months. That is the largest increase in over 16 years. According the CRA's discussion of the current state of the region's economy, the expansion is entering its third year, and based on the leading index, is expected to moderate over the next three to six months.

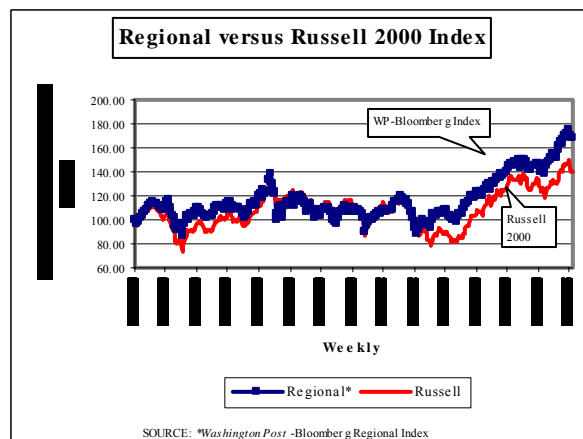




Of the four components that comprise the coincident index, the most dramatic growth occurred in the region's payroll employment. Since the beginning of 2004, employment averaged nearly 70,000 new jobs over a twelve-month period, an increase of 2.8 percent. The dramatic growth in new jobs contributed to the growth of retail sales which were up 7.3 percent in November and 7.8 percent for the year compared to 6.5 percent for the first eleven months of 2003.



The current strength of the region's labor market is in the service-providing sector. Because of the significant presence of the federal government in the region's economy both in direct labor and procurement, the service sector accounts for over 90 percent of total payroll jobs compared to the national average of 84 percent. Overall, service jobs increased 2.7 percent during 2004, and the largest gains occurred in the professional and business services sector ( $\uparrow 4.5\%$ ), and the retail trade sector ( $\uparrow 6.4\%$ ).



The region's unemployment rate at 3.1 percent in November remained one of the lowest among 51 metropolitan areas with a population of 1 million or more. Only Orange County, California, had a lower rate at 2.9 percent. That rate marked the first month since December 2001 that Orange County had a lower rate than the Washington metropolitan area.

Consumer spending in the region followed the national trend. Purchases of durable goods were up 5.4 percent in November and 6.8 percent for the year, while purchases of nondurable goods were up 8.8 percent in November and at a similar rate for the year. With the dramatic increase in new jobs, improved consumer confidence, and a strong real estate market in 2004, such trends are reflected in the retail sales of durable goods. The solid growth in retail sales is also reflected in retail sector jobs mentioned previously.

Because of the stellar performance in the regional economy, the financial performance of local companies has outperformed the nation's small businesses. For example, the *Washington Post-Bloomberg* regional stock index increased nearly 26 percent in 2004 compared to an 11 percent increase in the S&P 500 Index and 17 percent increase in the Russell 2000 Index. The more than double return in the regional index suggests

investors' confidence that the local economy will continue to outperform the national economy in the near term.

While employment, consumer confidence, and retail sales exhibited strong performance during 2004, the housing market also remained strong in spite of double-digit price increases over the past three years. Based on the Housing Price Index (HPI) developed by the Office of Federal Housing Enterprise Oversight (OFHEO), the index for the metropolitan region has increased at a double-digit rate fourteen out of sixteen quarters beginning with the fourth quarter of 2000. However, while prices experienced dramatic increases, construction of new homes has not kept pace with demand. According to CRA, indicators for future residential construction have moderated in recent months. While historically low mortgage interest rates have encouraged home sales, the supply of buildable lots in the region remains a major supply constraint. With building permits down 5.2 percent for the year, such decline suggests a continuation of price increases, albeit at moderating rates, because of the imbalance between supply and demand.

While the region's economy expanded at a stellar pace in 2004, Montgomery County's economy experienced mixed results during 2004. Highlights of the County's economic performance include:

- Retail sales as measured by sales tax receipts increased 7.9 percent in November and 6.5 for the first eleven months of 2004.
- Inflation accelerated in November with the overall rate at 3.6 percent in November and 2.8 percent for the year.
- The County's unemployment rate continues to be the lowest in the State and at 2.2 percent in November was below the region's (3.1%) and the State's (3.9%).
- Although construction permits for non-residential properties were up in December, the value of new construction projects were down dramatically (↓83.1%) over December of 2003. That decline suggests a slowdown in non-residential construction after the double-digit growth in 2004.
- The number of new residential projects declined for the fourth consecutive year and the number of single-family homes built in the County declined for the second year in a row.
- Median home prices were up 8.1 percent in December and 25.2 percent, or triple the national average, for 2004 compared to 13.2 percent the previous year.
- Housing sales were up 3.4% in December and 7.5% for the year and average prices continued their dramatic increase.

## **MONTGOMERY COUNTY ECONOMIC INDICATORS**

### ***Retail Sales***

Retail sales increased 7.9 percent in November compared to November 2003. For the first eleven months of 2004, sales in the County increased 6.5 percent compared to 3.8 percent the same period in 2003. That

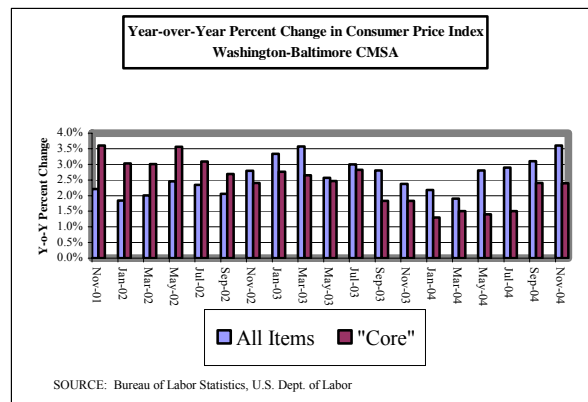
eleven-month rate was the largest since 1994 (↑7.6%).

The dramatic growth during 2004 was attributed to an improvement in the purchases of nondurable and durable goods. Sales of durable goods increased 9.1 percent during the first eleven months of 2004 compared to 3.2 percent for the same period during 2003. Purchases of nondurable goods increased 5.7 percent compared to 5.0 percent in 2003.

### *Inflation*

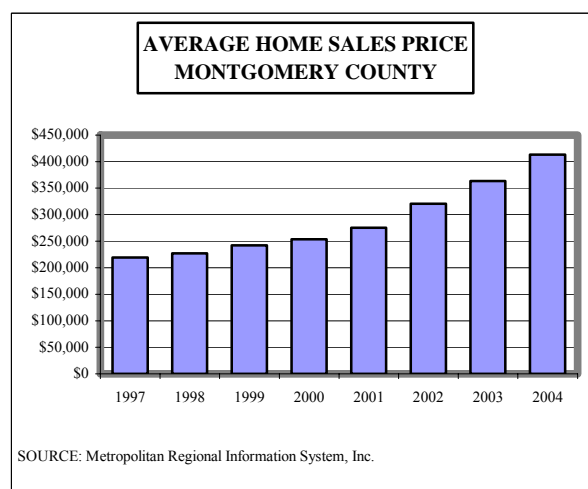
Inflation as measured by the Consumer Price index accelerated during 2004. At the beginning of 2004, consumer prices were running 2.2 percent above prices the year before. By November, inflation had risen to 3.6 percent for the twelve-month period, slightly higher than the national rate. Contributing to the rapid rise in consumer prices was energy (↑10.7%), largely attributed to gasoline prices (↑21.9%), and services (↑3.7%).

Consumer prices, excluding energy and food, also increased dramatically during 2004. At the start of the year, the “core” inflation rate was 1.8 percent. Since that time, the rate has increased to 2.4 percent for the twelve-month period ending in November. That increase is also higher than the national rate.



### *Residential Real Estate*

The real estate market in Montgomery County, particularly home sales, remained the economic story of 2004. Average prices continued their meteoric rise during the year reaching a December average of slightly over \$450,000, an increase of nearly \$50,000 since December 2003. For the year, average prices increased over 18 percent while median prices grew a dramatic 25 percent. Since December 1998, prices of homes in the County nearly doubled.



While average prices continued their dramatic rise, sales of homes increased 7 percent in 2004, up dramatically from the 3

percent in 2003 and the largest increase since 1999 ( $\uparrow 12.5\%$ ).

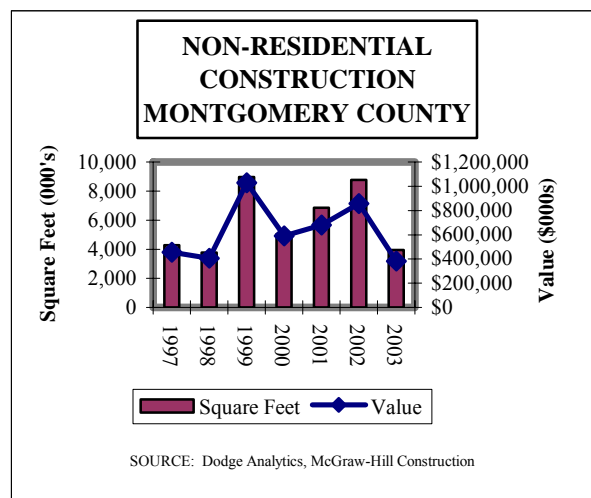
### ***Real Property Reassessments***

Because of the robust real estate market in the County, real property reassessments reached levels not seen since the late 1980s and 1990. Double-digit price increases over the past three years have resulted in rates reaching 55 percent and 65 percent in the past two years, respectively. The strong demand for condominiums has been on reason for such dramatic increases in reassessment rates. Between 1999 and 2003, sales of condominiums increased at an average annual rate of 13 percent with a majority of the sales occurring in the late 1990s, while sales of single-family homes increased at an average annual rate of slightly less than 3 percent during the same period. Over the 1999 to 2003 period, the average price of a condominium increased 85.0 percent compared to 70.4 percent for a two-bedroom single-family home. The market for condominiums has been so strong that for the first time in over ten years, the County received revenues from the condominium conversion transfer tax.

### ***Construction***

After experiencing a significant decline in 2003, construction activity in the County rebounded in 2004. Nonresidential construction experienced the more dramatic turnaround with permits up 41.2 percent in December and 9.3 percent for the year. The increase in the number of building permits for non-residential property suggests that the amount of additional capacity increased in 2004 and may continue into 2005. Although the total value of non-residential construction starts was down in December, it was up 27.1 percent for the

year compared to a decline of 46.5 percent in 2003.

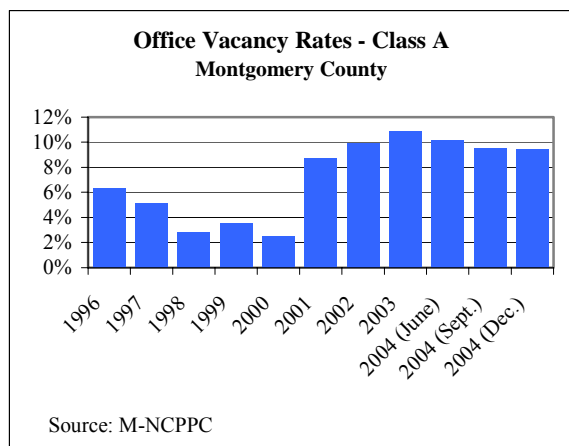


Non-residential construction added over 5 million square feet of capacity in 2004, up over 9 percent over the previous year. At the same time, the value of new non-residential construction was nearly \$600,000 or 27 percent above the value in 2003. Most of the new construction was for educational facilities, double the amount the previous year, and service stations and stores. However, construction of new office and bank buildings declined 35 percent in 2004. Overall, construction of commercial property added 285,000 square feet of space.

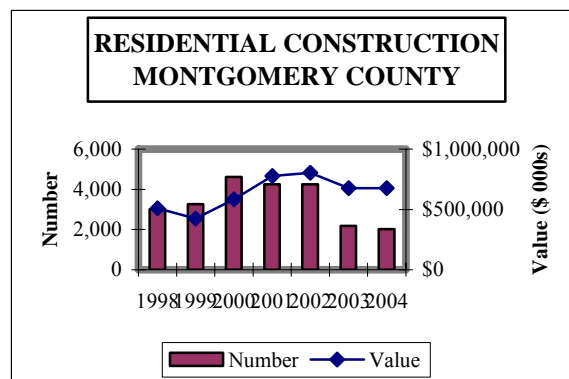
The decline in the rate of additional office and bank property is attributed to the vacancy rate for Class A in the County. Since 2000, the rate increased dramatically from 2.4 percent to 10.9 percent by December 2003, a fourfold increase. Since that time, the rate declined to 9.5 percent by December 2004. The rise in the vacancy rate between 2000 and 2002 matches the increase in new non-residential construction. With the drop in added capacity in 2003 and 2004, the imbalance between supply and



demand should diminish along with the vacancy rate assuming continued economic expansion.



However, unlike non-residential sector, residential construction did not improve in 2004. The number of residential permits declined nearly 17 percent for the first eleven months of 2004 compared to the same period in 2003. The value of new residential construction starts was up a meager 0.2 percent in 2004, a slight improvement compared to the 15.7 percent decline in 2003. The number of new single-family units built in 2004 was less than 1,700 compared to 2,100 units in 2003, a decline of 20 percent. The number of new units in 2004 was well below the 2000-2002 average of 4,250 and the lowest since 1997. With the significant drop in housing construction, the value of additional residential property also declined dramatically to its lowest level since 2000.



### ***Employment***

Average resident employment was 503,000 in 2004, an increase of 2.3 percent for the year. The labor force in the County continued to grow reaching an average for the year of approximately 515,000, an increase of 1.3 percent. Because employment grew faster than the labor force, the unemployment rate, which averaged 2.3 percent for the first eleven months of 2004 year, was lower than the 2.7 percent during the same period in 2003 and was considerably lower than the State's average of 4.1 percent and the national average of 5.5 percent.

Data for payroll employment to date cover only the first half of 2004 and reached nearly 455,000 in June, which was 0.7 percent higher than the adjusted 452,000 level experienced in June of 2003. The June 2004 data represent the second consecutive monthly increase of at least 3,700 new jobs. However, compared to the region, the growth of payroll jobs in Montgomery County are below the rates experienced by the Washington metropolitan area ( $\uparrow 2.8\%$ ) and the Maryland portion of the metropolitan area ( $\uparrow 1.8\%$ ) over the June 2003 to June 2004 period.

### ***Future Economic Performance***

CRA's leading index indicates a more moderate growth in the coming months. Based on a three-month moving average, the index has increased ten out of the past twelve months. While short-term interest rates are expected to increase 75 basis points through the first half of 2005, mortgage rates are not expected to increase significantly. However, while mortgage rates are expected to remain at low levels, the lack of a growing supply of new housing in the County will be unable to meet the potential growth in employment and households. As

such, home prices will continue to increase albeit at a slower pace. With the slowdown in residential construction, non-residential construction will be the important source of additional property in the County and a key to an increase in the County's assessable base. While the unemployment rate in the County is the lowest in the State, the meager increase in payroll employment the last three years and the first half of 2004 may be a drag on the County's economy and total personal income.

SELECTED ECONOMIC INDICATORS	Reporting Period	Current Period	Prior Year's Period	Year To-Date		2003
				2004	2003	
Leading Indicators						
National	Dec	0.2%		2.9%		3.0%
Washington MSA	Nov	-0.5%		2.3%		2.5%
Coincident Indicators						
National	Dec	0.3%		2.5%		1.6%
Washington MSA	Nov	-1.1%		7.0%		1.9%
Consumer Confidence Index						
National	Dec	10.5%		20.3%		17.5%
South Atlantic Region	Dec	4.7%		22.0%		16.5%
Consumer Sentiment (University of Michigan)	Dec	4.6%		8.6%		6.8%
Consumer Price Index						
All Items (nsa)						
National	Dec	3.3%		2.7%		2.3%
Washington - Baltimore CMSA	Nov	3.6%		2.8%		2.8%
Core CPI (nsa)						
National	Dec	2.2%		1.8%		1.5%
Washington - Baltimore CMSA	Nov	2.4%		1.7%		2.4%
Retail Trade						
National (sales - nsa)	Dec(p)	9.3%		8.0%		5.4%
Washington MSA (sales - nsa)	Nov	7.3%		7.8%		6.5%
Maryland (sales tax)	Nov	9.1%		9.0%		3.5%
Montgomery County (sales tax)	Nov	7.9%		6.5%		4.0%
Employment						
National (labor force data - nsa)	Dec	140,278,000	138,556,000	139,252,000	137,736,000	137,736,000
- Percent Change		1.2%		1.1%		0.9%
Washington PMSA (labor force data - nsa)	Nov	2,832,675	2,760,412	2,823,465	2,747,694	2,763,091
- Percent Change		2.6%		2.8%		1.6%
Montgomery County (labor force data)	Nov	506,512	493,932	503,503	492,350	495,052
- Percent Change		2.5%		2.3%		1.1%
Montgomery County (payroll)	June'04(p)	454,647	451,753	444,609	442,853	442,853
- Percent Change		0.6%		0.4%		0.5%
Unemployment						
National (nsa)	Dec	5.1%	5.4%	5.5%	6.0%	6.0%
Maryland (nsa)	Nov	3.9%	4.4%	4.1%	4.5%	4.3%
Washington PMSA	Nov	3.1%	3.3%	3.2%	3.6%	3.4%
Montgomery County	Nov	2.2%	2.6%	2.3%	2.7%	2.5%
Construction						
Construction Starts - Montgomery County						
Total (\$ thousand)	Dec	\$76,814	\$66,296	\$1,259,919	\$1,134,582	\$1,134,582
- Percent Change		15.9%		11.0%		-31.6%
Residential (\$ thousand)	Dec	\$72,274	\$39,396	\$677,705	\$676,613	\$676,613
- Percent Change		83.5%		0.2%		-15.7%
Non-Residential (\$ thousand)	Dec	\$4,540	\$26,900	\$582,214	\$457,969	\$457,969
- Percent Change		-83.1%		27.1%		-46.5%
Building Permits (Residential)						
National	Nov	151,399	127,189	1,866,586	1,714,757	1,862,365
- Percent Change		19.0%		8.9%		6.6%
Maryland	Nov	2,439	1,955	26,358	27,623	30,125
- Percent Change		24.8%		-4.6%		2.8%
Montgomery County	Nov	305	315	3,712	4,467	4,590
- Percent Change		-3.2%		-16.9%		-8.4%
Building Permits (Non-Residential)						
Montgomery County	Dec	161	114	1,966	1,798	1,798
- Percent Change		41.2%		9.3%		-3.2%
Real Estate						
National (saar)						
Sales	Nov	6,940,000	6,130,000	6,610,000	6,070,000	6,100,000
- Percent Change		13.2%		8.9%		9.6%
Median Price	Nov	\$188,200	\$170,500	\$181,918	\$168,536	\$170,000
- Percent Change		10.4%		7.9%		7.5%
Montgomery County						
Sales	Dec	1,493	1,444	17,771	16,534	16,534
- Percent Change		3.4%		7.5%		2.9%
Average Price	Dec	\$451,839	\$405,538	\$429,454	\$362,997	\$362,997
- Percent Change		11.4%		18.3%		13.2%
Median Price	Dec	\$351,437	\$325,000	\$369,900	\$295,500	\$295,500
- Percent Change		8.1%		25.2%		15.5%
Average Days on the Market	Dec	34	32	27	27	27

(p) = Preliminary

\*Data under 2004 and 2003 pertain to 2003 and 2002 respectively

### METROPOLITAN AREA OFFICE MARKET

#### Office Vacancy Rate by Jurisdiction and Class, 12/04

<i>Jurisdiction</i>	Class A	Class B	Class C	Total
Loudoun	14.10%	10.43%	2.07%	11.99%
Fairfax	10.74%	11.56%	5.67%	10.84%
Frederick	7.48%	9.55%	9.52%	8.55%
Alexandria/Arlington	8.09%	9.65%	17.55%	9.93%
<b>Montgomery</b>	<b>9.48%</b>	<b>8.42%</b>	<b>7.94%</b>	<b>8.87%</b>
District of Columbia	7.74%	5.33%	6.84%	6.76%
Prince George's	11.41%	10.49%	11.32%	11.01%
<i>Metropolitan Area</i>	9.35%	8.58%	9.58%	9.08%

#### Vacant Office Space Inventory by Jurisdiction and Class (sq.ft.)

<i>Jurisdiction</i>	Class A	Class B	Class C	Total
Loudoun	772,384	421,299	10,895	1,204,578
Fairfax	6,734,450	3,796,679	191,410	10,722,539
Frederick	161,763	176,005	47,917	385,685
Alexandria/Arlington	2,100,773	1,756,598	1,216,060	5,073,431
<b>Montgomery</b>	<b>2,746,471</b>	<b>2,228,740</b>	<b>483,788</b>	<b>5,458,999</b>
District of Columbia	4,793,027	2,292,083	848,675	7,933,785
Prince George's	1,030,840	936,888	379,727	2,347,455
<i>Region</i>	18,339,708	11,608,292	3,178,472	33,126,472

#### Office Space Inventory by Jurisdiction and Class (sq.ft.)

<i>Jurisdiction</i>	Class A	Class B	Class C	Total
Loudoun	5,478,511	4,037,667	527,395	10,043,573
Fairfax	62,680,183	32,831,926	3,375,950	98,888,059
Frederick	2,164,028	1,843,069	503,457	4,510,554
Alexandria/Arlington	25,974,328	18,194,275	6,930,828	51,099,431
<b>Montgomery</b>	<b>28,971,494</b>	<b>26,470,228</b>	<b>6,094,446</b>	<b>61,536,168</b>
District of Columbia	61,915,875	43,007,054	12,407,034	117,329,963
Prince George's	9,031,386	8,927,748	3,353,102	21,312,236
<i>Region</i>	196,215,805	135,311,967	33,192,212	364,719,984

#### Share of Office Space Inventory by Jurisdiction and Class

<i>Jurisdiction</i>	Class A	Class B	Class C	Total
Loudoun	54.5%	40.2%	5.3%	100.0%
Fairfax	63.4%	33.2%	3.4%	100.0%
Frederick	48.0%	40.9%	11.2%	100.0%
Alexandria/Arlington	50.8%	35.6%	13.6%	100.0%
<b>Montgomery</b>	<b>47.1%</b>	<b>43.0%</b>	<b>9.9%</b>	<b>100.0%</b>
District of Columbia	52.8%	36.7%	10.6%	100.0%
Prince George's	42.4%	41.9%	15.7%	100.0%
<i>Metropolitan Area</i>	53.8%	37.1%	9.1%	100.0%

Note:

Office Space inventory includes leasable and owner-occupied space.

Totals exclude non-classified space.

Vacant means "direct vacant" and does not include sublease space.

Source:

Montgomery County Department of Planning, Research and Technology Center  
Data compiled from Realty Information Group commercial space data file, 12/9/04